

COMMONWEALTH OF VIRGINIA
STATE CORPORATION COMMISSION

AT RICHMOND, JANUARY 30, 2004

COMMONWEALTH OF VIRGINIA, ex rel.

STATE CORPORATION COMMISSION

V.

CASE NO. SEC-2003-00041

MERRILL LYNCH, PIERCE, FENNER & SMITH, INCORPORATED,

DEFENDANT.

REC-2004-0130 P-2-23

EXHIBIT CONTINUED

SETTLEMENT ORDER

The Commission's Division of Securities and Retail Franchising ("Division") has instituted an investigation of Defendant, Merrill Lynch, Pierce, Fenner & Smith, Incorporated ("Merrill Lynch"), pursuant to § 13.1-518 of the Virginia Securities Act ("Act"), § 13.1-501 et seq. of the Code of Virginia.

As a result of its investigation, the Division alleges that Defendant, through its registered agents:

1. Recommended to Mr. and Mrs. Eugene Kallgren of Williamsburg, Virginia the purchase and sale of securities without reasonable grounds to believe that the recommendations were suitable for the investors, in violation of Commission Rule 21 VAC 5-20-280 A 3;
2. Failed to exercise diligent supervision over the securities activities of a broker-dealer agent employed at the Williamsburg, Virginia branch office of Merrill Lynch, in violation of Commission Rule 21 VAC 5-20-260 B;
3. Recommended to Ms. Julie R. Meals of Newport News, Virginia the purchase and sale of securities without reasonable grounds to believe that the recommendations were suitable for Ms. Meals, in violation of Commission Rule 21 VAC 5-20-280 A 3;

4. Failed to exercise diligent supervision over the securities activities of a broker-dealer agent employed at the York, Pennsylvania branch office of Merrill Lynch, in violation of Commission Rule 21 VAC 5-20-260 B.

The Defendant neither admits nor denies these allegations, but admits to the Commission's jurisdiction and authority to enter this settlement order.

As an offer to settle all matters arising from these allegations, Defendant has offered, and agreed to comply with, the following terms and undertakings:

1. Defendant will refrain from any conduct that constitutes a violation of the Act or the Commission's Rules promulgated thereunder;

2. Defendant, pursuant to § 13.1-521 of the Act, has agreed to offer to pay restitution to Mr. and Mrs. Eugene Kallgren in the amount of seventy three thousand five hundred forty-four dollars and eighty one cents (\$73,544.81). Defendant will make the aforesaid restitution offer to Mr. and Mrs. Eugene Kallgren within fifteen (15) calendar days of the entry of this settlement order and will provide satisfactory proof to the Division that the restitution offer has been made. Mr. and Mrs. Eugene Kallgren shall have thirty (30) calendar days from the date of receipt of the restitution offer to provide Defendant with written notification of their decision to accept or reject the restitution offer. If the offer of restitution is accepted, Defendant shall have fifteen (15) calendar days to deliver payment;

3. Defendant, pursuant to § 13.1-521 of the Act, has offered to pay restitution to Ms. Julie R. Meals in the amount of two hundred sixty-eight thousand seven hundred twenty-three dollars and twelve cents (\$268,723.12). Defendant made the aforesaid written restitution offer to Ms. Meals on August 12, 2003, and will provide satisfactory proof to the Division that the restitution offer and payment has been made;

4. Defendant, pursuant to § 13.1-521 of the Act, has agreed that the Division will engage a third party examiner, duly qualified, to conduct eight (8) branch examinations in the eastern third of the United States of America ("Third Party Examiner"). The Third Party Examiner must at least be a certified public accountant with three (3) years of experience in securities compliance management, or in the alternative, have five (5) years of experience in securities compliance management. If necessary, the Defendant and the Division will agree to other qualifications of the Third Party Examiner within fifteen (15) business days of the entry of this settlement order. Defendant shall recommend at least two (2) prospective firms, which meet such qualifications, to the Division for its consideration. Within thirty (30) business days of the date of receipt, if the Division has not accepted at least one (1) of the Defendant's recommendations, the matter will be referred to the Counsel to Commission for a final decision as to which Third Party Examiner, if any, should be utilized or if additional recommendations are warranted.

The Division will randomly select eight (8) branches located outside the Commonwealth of Virginia that employ Virginia registered broker-dealer agents for the special review. The Third Party Examiner will independently review and evaluate (1) Defendant's recommendations and clients' trading activity compared with customer's stated investment objectives and financial condition, (2) Defendant's written supervisory procedures regarding new accounts and securities transactions related to customer suitability, and (3) Defendant's separate system of review regarding the effective implementation of its supervisory procedures with regard to customer suitability. Defendant has agreed to compensate the Third Party Examiner for any and all costs of the examinations. Defendant shall pay such fees and charges directly to the Third Party Examiner within thirty (30) business days of receipt of the auditor's billing invoice. The Defendant and the Division, as described above, shall determine the scope of the examination.

5. It is recognized and understood that if Defendant fails to comply with any of the foregoing terms and undertakings, then the Commission reserves the right to take whatever action it deems appropriate, including, but not limited to, instituting a show cause proceeding under the Virginia Securities Act or other applicable statute based upon such failure to comply, on the allegations contained herein and/or on such other allegations as are warranted, and Defendant will not contest the exercise of the right reserved.

The Division has recommended that Defendant's offer of settlement be accepted pursuant to the authority granted to the Commission in § 12.1-15 of the Code of Virginia.

NOW, THEREFORE, IT IS ORDERED THAT:

1. Pursuant to the authority granted to the Commission in § 12.1-15 of the Code of Virginia, Defendant's offer of settlement is accepted;

2. Defendant fully complies with the aforesaid terms and undertakings of the settlement;

3. The Commission shall retain jurisdiction in this matter for all purposes, including the institution of a show cause proceeding as described above, or taking such other action it deems appropriate, on account of Defendant's failure to comply with the terms and undertakings of the settlement.

AN ATTESTED copy hereof shall be sent by CERTIFIED MAIL, RETURN RECEIPT REQUESTED, to Mr. Andrew Kandel, First Vice-President/Assistant General Counsel, Merrill Lynch, Pierce, Fenner & Smith, Inc., Office of General Counsel, 222 Broadway, 13th Floor, New York, New York 10038; Ms. Elizabeth Hoop Fay, Esquire, Morgan, Lewis & Bockius, LLP, 1701 Market Street, Philadelphia, Pennsylvania 19103; and Mr. John S. Barr, Esquire, McGuire Woods, LLP, 901 East Cary Street, Richmond, Virginia 23219.

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MERRILL LYNCH, PIERCE, FENNER &
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DEFENDANT

ADMISSION AND CONSENT

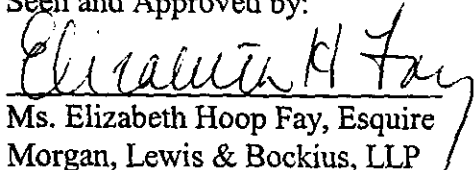
The Defendant, Merrill Lynch, Pierce, Fenner & Smith Inc., admits to the jurisdiction of the State Corporation Commission of Virginia as to the party and the subject matter hereof and, without admitting or denying the allegations made herein by the Division of Securities and Retail Franchising, hereby consents to the form, substance and entry of the foregoing Settlement Order.

The Defendant further states that no offer, tender, threat or promise of any kind whatsoever has been made by the Commission or any member, subordinate, employee, agent or representative thereof in consideration of the foregoing Settlement Order.

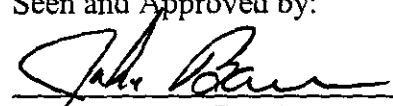
Dated: January 14, 2004


Andrew Kandel, Esquire
First Vice-President/Assistant General
Counsel
Merrill Lynch, Pierce, Fenner & Smith Inc.

Seen and Approved by:


Ms. Elizabeth Hoop Fay, Esquire
Morgan, Lewis & Bockius, LLP
1701 Market Street
Philadelphia, PA 19103

Seen and Approved by:


Mr. John Barr, Esquire
McGuire Woods, LLP
901 East Cary Street
Richmond, VA 23219